DEC 20 1952

IN THE

Supreme Court of the United States

OCTOBER TERM, 1952

No. 464

FIRST NATIONAL BANK IN HOUSTON, P. P. BUTLER, T. W. GREGORY, JR., LEON JAWORSKI AND B. J. BRADSHAW,

Petitioners,

VS.

CHARLES M. LAKE, TRUSTEE OF PETROL TERMINAL CORPORATION AND SUBSIDIARY CORPORATIONS, IN PROCEEDINGS FOR REORGANIZATION,

Respondent.

BRIEF FOR RESPONDENT IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

FRANK B. OBER,
640 Mathieson Bldg.,
Baltimore 2, Md.
Counsel for Respondent.

The Daily Record Co., Baltimore 3, Md.

INDEX

TABLE OF CONTENTS

PAGE

STATEMENT 2

ARGUMENT:

I. The questions alleged by the Petitioner to be presented are not necessarily raised by the record, since the decision must be sustained in any event on other grounds 4

A. The extent of the summary power of the reorganization court as opposed to that of a straight bankruptcy court is not necessarily involved here, since on the face of the record the Bank has no substantially adverse claim but merely a colorable one 4

B. The Texas Court manifestly had no in rem jurisdiction over the assigned rights in the contract between debtor and The California Oil Company, and since the attempt to "quiet title" to the contract was without basis, the reorganization court had jurisdiction to prevent such harassment 6

C. Even if sustained, the pledge of the stock of the subsidiaries merely represents junior claims against assets being administered in the United States District Court in Maryland, over which that Court has exclusive jurisdiction 7

II. If the questions raised by the Petitioner should ever be reached by this Court, then under the explicit provisions of Chapter X of the Bankruptcy Act, as uniformly construed by this and other courts, the decision below is the only possible decision, and no new and novel question is presented to this Court 9

CONCLUSION 13

Table of Citations

Cases

	PAGE
Bardes v. First National Bank, 178 U. S. 524 (1900)	10
Continental Illinois National Bank & Trust Co. v. Chicago, Rock Island & Pac. Ry. Co., 294 U. S. 648 (1935)	10, 12
Cuyahoga Finance Co., In re, 6th Cir., 136 F. 2d 18 (1943)	10
Jellenik v. Huron Copper Mining Co., 177 U. S. 1 (1900)	8
May v. Henderson, 268 U. S. 111, 117 (1925)	7
McQuillen v. National Cash Register Co., 4 Cir., 112 F. 2d 877 (1940); cert. den. 311 U. S. 695 (1940)	8
Taubel-Scott-Kitzmiller Co. v. Fox, 264 U. S. 426, 433 (1924)	4, 10
Williams v. Austrian, 331 U. S. 642 (1947)	10

Statutes

Title 11, U. S. C.	
Section 202	7
205	12
511	8, 11
529	8
548	12
596	8, 12
597	8, 12
616	8, 11
624	9
625	12

Other Authorities

Gerdes on Corporate Reorganization, Sec. 855	11

IN THE

Supreme Court of the United States

OCTOBER TERM, 1952

No. 464

FIRST NATIONAL BANK IN HOUSTON, P. P. BUTLER, T. W. GREGORY, JR., LEON JAWORSKI AND B. J. BRADSHAW,

Petitioners,

VS.

CHARLES M. LAKE, TRUSTEE OF PETROL TERMINAL CORPORATION AND SUBSIDIARY CORPORATIONS, IN PROCEEDINGS FOR REORGANIZATION,

Respondent.

BRIEF FOR RESPONDENT IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

Charles M. Lake, Trustee of Petrol Terminal Corporation and subsidiaries, Respondent herein, submits herewith his brief in opposition to the Petition praying that a writ of certiorari issue to review the judgment entered in this cause on October 7, 1952, by the United States Court of Appeals for the Fourth Circuit.

STATEMENT

Respondent calls attention to the following facts which Respondent deems relevant and which were either omitted entirely or inadequately stated in the Petition:

The pledge to the Bank of "certain shares of stock held by them in other corporations", referred to on page 3 of the Petition, was of stock in two subsidiary corporations of the principal debtor, and the United States District Court in Maryland has taken jurisdiction over such subsidiaries and their assets (R. 87 ff). These two subsidiaries are Automotive Service of Reading, Inc. and Lehigh Valley Oil Company, Inc. (hereinafter respectively called "Automotive" and "Lehigh").

"Marketers", referred to on the same page of the Petition, had been held to be a mere corporate shell and identical with Terminal (R. 2).

The assignment to the Bank of the contract (referred to by Petitioners in the third paragraph of the same page) as additional collateral on May 29, 1951, was taken the *same day* that the initial involuntary petition in bankruptcy was filed against the debtor, and the assignment of the stock above referred to was but forty days prior to such bankruptcy and was an assignment of the entire stock interest of the debtor in the said two subsidiaries (R. 4). There is no claim that any new consideration was furnished for these assignments, which were taken merely as additional collateral for a long overdue debt. On the undisputed allegations of the petition to the District Court, on which the injunction was issued (R. 1-17), such assignments were not in the ordinary course of business, but were made after the Bank had convincing evidence that the debtor was in desperate financial condition, had borrowed huge sums on fraudulent financial statements and bogus invoices, and had

been issuing bad checks and kiting accounts receivable (R. 4-5).

The so-called "quiet title" action was brought in Texas against this Respondent as Trustee, without the consent of the United States District Court in Maryland which had appointed him (R. 9). It was brought in the teeth of a broad injunction, which is in the customary form for an order approving reorganization proceedings, and which enjoins everyone from interfering with the property and assets of the debtor or interfering with the exclusive jurisdiction of the Court (R. 91). Petitioners had been given specific notice of such injunction by registered mail (R. 8).

The Bank had knowledge of the reorganization proceedings from their inception and has received notices of the various steps taken therein, including the order fixing the time and method of filing claims against the debtor and its subsidiaries (R. 7), but the Bank has not attempted to file any claim, whether as secured or unsecured creditor or stockholder against the debtor or its instrumentality, Marketers, or any of its subsidiaries (R. 8).

The Petitioners were given a full opportunity to be heard by the United States District Court in Maryland and elected to appear specially to contest the jurisdiction only and at no time have pleaded to the merits of the injunction petition or put in issue the facts alleged therein. The original injunction (R. 17-20), which was continued in the order overruling the Bank's motion to dissolve on jurisdictional grounds (R. 37-38), was limited to prohibiting further steps in the Texas suit or further suits against the Trustee or attempts to enforce liens on the stock of Automotive and Lehigh without the prior consent of the Court.

ARGUMENT

POINT I

THE QUESTIONS ALLEGED BY THE PETITIONERS TO BE PRESENTED ARE NOT NECESSARILY RAISED BY THE RECORD, SINCE THE DECISION MUST BE SUSTAINED IN ANY EVENT ON OTHER GROUNDS.

A. The extent of the summary power of the reorganization court as opposed to that of a straight bankruptcy court is not necessarily involved here, since on the face of the record the Bank has no substantially adverse claim but merely a colorable one.

Petitioners elected to appear specially below and test the validity of the injunction solely on a motion to dismiss. In this manner they attempted to raise a jurisdictional question and at the same time circumvent the undoubted power of a bankruptcy court (even aside from Chapter X proceedings) to determine whether a claim is substantially adverse or merely colorable, as a part of the determination it must make as to its own jurisdiction. See *Taubel-Scott Kitzmiller Co. v. Fox,* 264 U. S. 426, 433 (1924). Had Petitioners wished to avoid the summary jurisdiction of the reorganization court, they should have raised the question by joining issue in that court on the facts which on the pleadings indicate that the Bank's claim is not substantially adverse.

Thus, the following facts, alleged in the petition requesting an injunction, and on the basis of which the injunction was granted, must be accepted as true for the purposes of this action:

> (R. 2) "Marketers has subsequently been held to be the corporate shell and identical with Terminal. . . ."
>
> (R. 4, 5) "The Houston Bank has not filed any claim herein, either as a secured or an unsecured creditor, but obtained possession from Terminal on April 13, 1951,

about forty days prior to these proceedings, of all of the certificates representing its entire stock interest in Automotive and Lehigh under agreements, copies of which are filed herewith as Petitioner's Exhibit No. 5. On May 29, 1951, the date of Terminal's bankruptcy, the Bank obtained an assignment of a contract under which some $250,000 will become payable to Marketers by the California Oil Company over a period of years, filed herewith as Petitioner's Exhibit No. 6; that said transfers were not in due course of business, but as security for indebtedness of Terminal and Marketers long overdue, when the Houston Bank had convincing evidence of their desperate financial condition through knowledge that they had borrowed huge sums on fraudulent financial statements, bogus invoices, had been issuing bad checks, kiting accounts receivable, and of other facts indicating that such transfers would constitute voidable preferences if bankruptcy ensued within four months."

The District Court judge himself, during the initial hearing, suggested that the Bank's by-passing of the reorganization court could only mean that it felt it was on such "shaky" ground that it would rather try to maintain its position in its local jurisdiction (R. 85).

In the light of such facts it is manifest that the Bank's claim is merely colorable. Therefore, even if, as contended by Petitioners and contrary to the opinion below, the ordinary bankruptcy rule as to jurisdiction were applicable here, the Bank would not be entitled to have the issues determined in a plenary action. Nor is there any reason why the Bank should be able to reach the same result by its wholly unprecedented scheme of bringing a "quiet title" action in another district and thus preventing the Bankruptcy Court from determining whether the claim was so substantial as to deprive it of summary jurisdiction.

B. The Texas Court manifestly had no in rem jurisdiction over the assigned rights in the contract between debtor and The California Oil Company, and since the attempt to "quiet title" to the contract was without basis, the reorganization court had jurisdiction to prevent such harassment.

While the lower court chose to put its decision on the broadest jurisdictional grounds, it pointed out (R. 109) a number of alternative grounds which raised grave questions, particularly the question whether the contract involved had such a situs in Texas as to authorize an action *in rem*. That choses in action have no situs for the purpose of an action *in rem* is elementary. Manifestly Petitioners attempted to use this unprecedented "quiet title" action because neither the Trustee, Terminal, nor California Oil Company could be sued *in personam* in Texas. Under the procedure invoked by Petitioners a writ issued out of the Texas Court, and process was served upon Respondent in Maryland (R. 9).

Moreover the consent of the Maryland District Court was not sought before this action was brought against its duly appointed officer, the Trustee — another "grave" question that the lower court referred to but found unnecessary to decide (R. 109).

It should also be noted that an independent and equally insurmountable barrier to the Bank's Texas action is based upon the conceded fact that Terminal (and Marketers has been held to be identical therewith) went into bankruptcy on May 29, 1951, the date of the assignment of the contract. Neither in its so-called "quiet title" action (R. 21-28) nor in its motion to dissolve the injunction (R. 28-36) does the Bank assert any claim that it received the assignment earlier

on May 29, 1951 than the initial petition in bankruptcy was filed against the debtor, or even that it received the assignment at all the same day it was dated. Since the Trustee's prima facie title to a chose in action under 11 U. S. C. 110 a (5) and (6) arises on the date of the filing of the petition, such an allegation would be essential (even assuming that fractions of a day would be material) to a claim that the assignment by the debtor was valid in spite of bankruptcy. The assignment was, therefore, void as a transfer by the bankrupt of assets after a petition in bankruptcy had been filed. *May v. Henderson*, 268 U. S. 111, 117 (1925).

Entirely aside from any question of preference, Petitioners' suit is no more than an attempt to involve the Trustee, through the medium of a novel "quiet title" action in expensive piecemeal litigation in Texas where jurisdiction is manifestly lacking. It involves only a part of the evidence which may become material in a later *in personam* contract action which has to be brought in a district where the obligor on the contract can be found. Defending such an action in another court would impede the orderly progress of the reorganization, including the working out of proper setoffs to claims, as pointed out by the lower court (R. 100). If reorganization is to be a practicable means of dealing with the affairs of a debtor, such harassment to no purpose must be properly enjoinable.

C. Even if sustained, the pledge of the stock of the subsidiaries merely represents junior claims against assets being administered in the United States District Court in Maryland, over which that Court has exclusive jurisdiction.

The jurisdiction of the Texas Court cannot be sustained by the mere fact that the Bank possesses stock certificates, title to which are in the debtor. *In rem* jurisdiction over

shares of stock is not conferred by the mere presence of the certificates themselves. *Jellenik v. Huron Copper Mining Co.*, 177 U. S. 1 (1900); *McQuillen v. National Cash Register Co.*, 4 *Cir.*, 112 F. 2d 877 (1940); cert. den. 311 U. S. 695 (1940); see also lower court comment (R. 109). Here, the stock ledgers are located in Maryland (R. 3, 4).

Nowhere in their Petition do Petitioners refer to the fact that the certificates of stock in the Bank's hands represent stock owned by Terminal in subsidiary companies which are being reorganized together with their parent in the same proceeding in Maryland. Such stock, therefore, represents merely a claim (junior to that of creditors) against assets under the exclusive jurisdiction of the Maryland District Court. As the lower court said (R. 100):

> "And, most important of all, since the establishment of the validity of the pledge would fix the lien of the pledge on the property, this would take from the reorganization court power to determine the status of that property. This is of the greatest importance here, since the shares of stock pledged were shares in subsidiary corporations which were being reorganized in the proceeding presently before the Court."

Inasmuch as the reorganization court is given exclusive jurisdiction of the debtor and its property wherever located (11 U. S. C. Sec. 511), and the properties of the subsidiaries whose stock was held under the alleged pledge were under the jurisdiction of the Maryland District Court which had taken jurisdiction of them as well as of the parent corporation under the provisions of Sec. 129 of Chapter X (11 U. S. C. Sec. 529), that Court had complete power to require proof of and determine the status not only of the creditors but also of stockholders (11 U. S. C. Sec. 596-597; 616 (1) and (2)). A reorganization plan is made binding upon both creditors and stockholders whether

their claims have been scheduled or allowed or not (See 624 (1) and (4)). Nor is there any indication in the statute that a creditor who is *pledgee* of the stock of corporations, assets of which are being administered in the reorganization court, is entitled to an exemption from its broad jurisdiction not accorded either ordinary creditors or stockholders.

Point Two

IF THE QUESTIONS RAISED BY THE PETITIONER SHOULD EVER BE REACHED BY THIS COURT, THEN UNDER THE EXPLICIT PROVISIONS OF CHAPTER X OF THE BANKRUPTCY ACT AS UNIFORMLY CONSTRUED BY THIS AND OTHER COURTS, THE DECISION BELOW IS THE ONLY POSSIBLE DECISION, AND NO NEW AND NOVEL QUESTION IS PRESENTED TO THIS COURT.

At the outset it should be stated that the alleged three questions presented, as framed by Petitioners (Petition p. 2), are stated in a highly misleading manner, in that in each there is the implication that a question of title is involved. The fact is that on the face of the record it is alleged by Respondent in the petition for injunction in several places (R. 4, 5, 10), and admitted a number of times by Petitioners themselves (R. 29, 30, 33, 44) that the Bank claims to hold as pledgee only. The Petition attempts to set up issues not presented by these facts nor decided by the lower court. The true question presented by this case was aptly stated by Judge Parker in the opinion of the lower court (R. 98):

> "The question involved in the case is not whether the reorganization court in a Chapter X proceeding has summary jurisdiction of a suit to recover property claimed adversely by the holder thereof; but whether a secured creditor may, through the device of asking a declaratory judgment, take away the jurisdiction of the reorganization court over the property of the debtor pledged as security and may likewise take away

> from that court the jurisdiction to determine the amount of secured and unsecured debts of the creditor entitled to share in any plan of reorganization that the court may approve."

Petitioners' failure to distinguish between the interest of a creditor claiming to hold property as security and the interest of a non-resident holding both possession and a claim to *title* is responsible for a large part of Petitioners' argument. The cases cited on page 8 of the Petition to support the contention that the reorganization court did not have summary jurisdiction over this property of the debtor are all cases involving claims to *title* and have been distinguished as such by the lower court (R. 101, 103, 108). The *Taubel-Scott-Kitzmiller Co.* and *Bardes* cases relied on by Petitioners (pp. 6, 8), both involve ordinary bankruptcy situations and can hardly be considered authority for determining the extent of the broadened summary jurisdiction of the reoganization court. *Williams v. Austrian* (p. 8) was in no way concerned with the summary jurisdiction of the reorganization court, the holding merely being that lower Federal courts had jurisdiction to hear plenary suits brought by a reorganization trustee even though diversity or the other usual grounds for Federal jurisdiction were lacking.

Petitioners' statement (p. 10) that the distinction made by the majority opinion "is without support in a single reported case" completely ignores the cases cited by the majority opinion (R. 99-102), especially *Continental Illinois National Bank & Trust Co. v. Chicago, Rock Island & Pac. Ry. Co.*, 294 U. S. 648 (1935) and *In re Cuyahoga Finance Co.*, 6th Cir., 136 F. 2d 18 (1943). The minority opinion does not recognize this distinction (R. 119). But this is the distinction laid down by Congress, which gives the

reorganization court "the exclusive jurisdiction of the debtor and its property wherever located" (11 U. S. C. Sec. 511). This language inevitably makes jurisdiction depend on title (see *Gerdes on Corporate Reorganization,* Sec. 855) and contains no exception in favor of claimants to liens thereon. On the contrary, the very purpose of Chapter X (and in fact a fundamental difference from ordinary bankruptcy and Chapter XI proceedings) is to make subject to the jurisdiction of the court mortgage and lien creditors of all types. Numerous provisions in the statute provide for the alteration of the rights of secured creditors, the cancellation of their liens and the like (e. g. 11 U. S. C. 616 (1), (10)). There is no statutory basis whatsoever for exempting from the reorganization court's jurisdiction a pledgee any more than a mortgagee or other lien creditor; nor for permitting secured creditors to have other courts decide the amount of their claims or the setoffs thereto or the validity or priority of their security. It would be manifestly absurd to make such exceptions merely because a creditor claims that there may be some doubt as to the validity of the lien he claims. To permit any exceptions at all to the exclusive jurisdiction of the reorganization court over the debtor and its property and all claims thereto, whether of stockholders or creditors, would make it impracticable ever to reorganize and would destroy the effectiveness of Chapter X.

The argument in the Petition is largely based on the dissenting Judge's opinion and particularly on that portion which contains the unsupported assertion, without citing Section 511 *supra,* that there is no difference in principle between claims of third persons to title and claims of a creditor to security (R. 119). This ignores the language of Section 511, which gives the court "exclusive jurisdiction of the debtor and *its property* wherever located". This sec-

tion, however, does not go on to add "and over suits to recover property held by, or claims against third persons" or similar language which would have created the all inclusive jurisdiction which the dissenting Judge below seemed to think resulted from the majority holding.

Even under the railroad reorganization section of the Bankruptcy Act (11 U. S. C. Sec. 205) and before the addition by Chapter X of many provisions enlarging the summary jurisdiction of the reorganization court (e. g., 11 U. S. C. Secs. 548, 596, 597, 625), this Court had held that a sale of collateral by a non-resident holder was properly enjoinable in summary proceedings. *Continental Illinois National Bank & Trust Co. v. Chicago, Rock Island & Pacific Railway Co.*, 294 U. S. 648 (1935).

The very purpose of Chapter X, as shown by its history and the decisions construing it, is to require creditors, including secured creditors, to sit around the table with each other in the reorganization court and work out the best possible plan for the benefit of all. Such procedure would be completely ineffective if a creditor could circumvent it by securing piecemeal decisions in other forums as to property of the debtor or as to a part of a creditor's claim under the guise of a quiet title action.

Especially is it necessary that a single centralized forum decide all such questions as to property of the debtor where the collateral involved is stock of subsidiary corporations themselves under the exclusive jurisdiction of the reorganization court (a point completely ignored by the minority opinion in stating the question here involved, R. 119).

CONCLUSION

For the reasons stated Respondent urges this Court to deny Petitioners' application for a writ of certiorari.

Respectfully submitted,

FRANK B. OBER,

Counsel for Respondent.